THIRD DIVISION

[G.R. No. 156940. December 14, 2004]

ASSOCIATED BANK (Now WESTMONT BANK), *petitioner, vs.* VICENTE HENRY TAN, *respondent*.

D E C I S I O N

PANGANIBAN, *J.:*

While banks are granted by law the right to debit the value of a dishonored check from a depositors account, they must do so with the highest degree of care, so as not to prejudice the depositor unduly.

The Case

Before us is a Petition for Review[1] under Rule 45 of the Rules of Court, assailing the January 27, 2003 Decision[2] of the Court of Appeals (CA) in CA-GR CV No. 56292. The CA disposed as follows:

WHEREFORE, premises considered, the Decision dated December 3, 1996, of the Regional Trial Court of Cabanatuan City, Third Judicial Region, Branch 26, in Civil Case No. 892-AF is hereby **AFFIRMED**. Costs against the [petitioner].[3]

The Facts

The CA narrated the antecedents as follows:

Vicente Henry Tan (hereafter TAN) is a businessman and a regular depositor-creditor of the Associated Bank (hereinafter referred to as the BANK). Sometime in September 1990, he deposited a postdated UCPB check with the said BANK in the amount of ₱101,000.00 issued to him by a certain Willy Cheng from Tarlac. The check was duly entered in his bank record thereby making his balance in the amount of ₱297,000.00, as of October 1, 1990, from his original deposit of ₱196,000.00. Allegedly, upon advice and instruction of the BANK that the ₱101,000.00 check was already cleared and backed up by sufficient funds, TAN, on the same date, withdrew the sum of ₱240,000.00, leaving a balance of ₱57,793.45. A day after, TAN deposited the amount of ₱50,000.00 making his existing balance in the amount of ₱107,793.45, because he has issued several checks to his business partners, to wit:

CHECK NUMBERS DATE AMOUNT

a. 138814 Sept. 29, 1990 ₱9,000.00
b. 138804 Oct. 8, 1990 9,350.00
c. 138787 Sept. 30, 1990 6,360.00
d. 138847 Sept. 29, 1990 21,850.00
e. 167054 Sept. 29, 1990 4,093.40

f. 138792 ` Sept. 29, 1990 3,546.00
g. 138774 Oct. 2, 1990 6,600.00
h. 167072 Oct. 10, 1990 9,908.00
i. 168802 Oct. 10, 1990 3,650.00

However, his suppliers and business partners went back to him alleging that the checks he issued bounced for insufficiency of funds. Thereafter, TAN, thru his lawyer, informed the BANK to take positive steps regarding the matter for he has adequate and sufficient funds to pay the amount of the subject checks. Nonetheless, the BANK did not bother nor offer any apology regarding the incident. Consequently, TAN, as plaintiff, filed a Complaint for Damages on December 19, 1990, with the Regional Trial Court of Cabanatuan City, Third Judicial Region, docketed as Civil Case No. 892-AF, against the BANK, as defendant.

In his [C]omplaint, [respondent] maintained that he ha[d] sufficient funds to pay the subject checks and alleged that his suppliers decreased in number for lack of trust. As he has been in the business community for quite a time and has established a good record of reputation and probity, plaintiff claimed that he suffered embarrassment, humiliation, besmirched reputation, mental anxieties and sleepless nights because of the said unfortunate incident. [Respondent] further averred that he continuously lost profits in the amount of ₱250,000.00. [Respondent] therefore prayed for exemplary damages and that [petitioner] be ordered to pay him the sum of ₱1,000,000.00 by way of moral damages, ₱250,000.00 as lost profits, ₱50,000.00 as attorneys fees plus 25% of the amount claimed including ₱1,000.00 per court appearance.

Meanwhile, [petitioner] filed a Motion to Dismiss on February 7, 1991, but the same was denied for lack of merit in an Order dated March 7, 1991. Thereafter, [petitioner] BANK on March 20, 1991 filed its Answer denying, among others, the allegations of [respondent] and alleged that no banking institution would give an assurance to any of its client/depositor that the check deposited by him had already been cleared and backed up by sufficient funds but it could only presume that the same has been honored by the drawee bank in view of the lapse of time that ordinarily takes for a check to be cleared. For its part, [petitioner] alleged that on October 2, 1990, it gave notice to the [respondent] as to the return of his UCPB check deposit in the amount of ₱101,000.00, hence, on even date, [respondent] deposited the amount of ₱50,000.00 to cover the returned check.

By way of affirmative defense, [petitioner] averred that [respondent] had no cause of action against it and argued that it has all the right to debit the account of the [respondent] by reason of the dishonor of the check deposited by the [respondent] which was withdrawn by him prior to its clearing. [Petitioner] further averred that it has no liability with respect to the clearing of deposited checks as the clearing is being undertaken by the Central Bank and in accepting [the] check deposit, it merely obligates itself as depositors collecting agent subject to actual payment by the drawee bank. [Petitioner] therefore prayed that [respondent] be ordered to pay it the amount of ₱1,000,000.00 by way of loss of goodwill, ₱7,000.00 as acceptance fee plus ₱500.00 per appearance and by way of attorneys fees.

Considering that Westmont Bank has taken over the management of the affairs/properties of the BANK, [respondent] on October 10, 1996, filed an Amended Complaint reiterating substantially his allegations in the original complaint, except that the name of the previous defendant ASSOCIATED BANK is now WESTMONT BANK.

Trial ensured and thereafter, the court rendered its Decision dated December 3, 1996 in favor of the [respondent] and against the [petitioner], ordering the latter to pay the [respondent] the sum of ₱100,000.00 by way of moral damages, ₱75,000.00 as exemplary damages, ₱25,000.00 as attorneys fees, plus the costs of this suit. In making said ruling, it was shown that [respondent] was not officially informed about the debiting of the ₱101,000.00 [from] his existing balance and that the BANK merely allowed the [respondent] to use the fund prior to clearing merely for accommodation because the BANK considered him as one of its valued clients. The trial court ruled that the bank manager was negligent in handling the particular checking account of the [respondent] stating that such lapses caused all the inconveniences to the [respondent]. The trial court also took into consideration that [respondents] mother was originally maintaining with the x x x BANK [a] current account as well as [a] time

deposit, but [o]n one occasion, although his mother made a deposit, the same was not credited in her favor but in the name of another.[4]

Petitioner appealed to the CA on the issues of whether it was within its rights, as collecting bank, to debit the account of its client for a dishonored check; and whether it had informed respondent about the dishonor prior to debiting his account.

Ruling of the Court of Appeals

Affirming the trial court, the CA ruled that the bank should not have authorized the withdrawal of the value of the deposited check prior to its clearing. Having done so, contrary to its obligation to treat respondents account with meticulous care, the bank violated its own policy. It thereby took upon itself the obligation to officially inform respondent of the status of his account before unilaterally debiting the amount of ₱101,000. Without such notice, it is estopped from blaming him for failing to fund his account.

The CA opined that, had the ₱101,000 not been debited, respondent would have had sufficient funds for the postdated checks he had issued. Thus, the supposed accommodation accorded by petitioner to him is the proximate cause of his business woes and shame, for which it is liable for damages.

Because of the banks negligence, the CA awarded respondent moral damages of ₱100,000. It also granted him exemplary damages of ₱75,000 and attorneys fees of ₱25,000.

Hence this Petition.[5]

Issue

In its Memorandum, petitioner raises the sole issue of whether or not the petitioner, which is acting as a collecting bank, has the right to debit the account of its client for a check deposit which was dishonored by the drawee bank.[6]

The Courts Ruling

The Petition has no merit.

Sole Issue:
Debit of Depositors Account

Petitioner-bank contends that its rights and obligations under the present set of facts were misappreciated by the CA. It insists that its right to debit the amount of the dishonored check from the account of respondent is clear and unmistakable. Even assuming that it did not give him notice that the check had been dishonored, such right remains immediately enforceable.

In particular, petitioner argues that the check deposit slip accomplished by respondent on September 17, 1990, expressly stipulated that the bank was obligating itself merely as the depositors collecting agent and -- until such time as actual payment would be made to it -- it was reserving the right to charge against the depositors account any amount previously credited. Respondent was

allowed to withdraw the amount of the check prior to clearing, merely as an act of accommodation, it added.

At the outset, we stress that the trial courts factual findings that were affirmed by the CA are not subject to review by this Court.[7] As petitioner itself takes no issue with those findings, we need only to determine the legal consequence, based on the established facts.

Right of Setoff

A bank generally has a right of setoff over the deposits therein for the payment of any withdrawals on the part of a depositor.[8] The right of a collecting bank to debit a clients account for the value of a dishonored check that has previously been credited has fairly been established by jurisprudence. To begin with, Article 1980 of the Civil Code provides that [f]ixed, savings, and current deposits of money in banks and similar institutions shall be governed by the provisions concerning simple loan.

Hence, the relationship between banks and depositors has been held to be that of creditor and debtor.[9] Thus, legal compensation under Article 1278[10] of the Civil Code may take place when all the requisites mentioned in Article 1279 are present,[11] as follows:

(1) That each one of the obligors be bound principally, and that he be at the same time a principal creditor of the other;
(2) That both debts consist in a sum of money, or if the things due are consumable, they be of the same kind, and also of the same quality if the latter has been stated;
(3) That the two debts be due;
(4) That they be liquidated and demandable;
(5) That over neither of them there be any retention or controversy, commenced by third persons and communicated in due time to the debtor.[12]

Nonetheless, the real issue here is not so much the right of petitioner to debit respondents account but, rather, the manner in which it exercised such right. The Court has held that even while the right of setoff is conceded, separate is the question of whether that remedy has properly been exercised.[13]

The liability of petitioner in this case ultimately revolves around the issue of whether it properly exercised its right of setoff. The determination thereof hinges, in turn, on the banks role and obligations, *first*, as respondents depositary bank; and *second*, as collecting agent for the check in question.

Obligation as Depositary Bank

In *BPI v. Casa Montessori*,[14] the Court has emphasized that the banking business is impressed with public interest. Consequently, the highest degree of diligence is expected, and high standards of integrity and performance are even required of it. By the nature of its functions, a bank is under obligation to treat the accounts of its depositors with meticulous care.[15]

Also affirming this long standing doctrine, *Philippine Bank of Commerce v. Court of Appeals*[16] has held that the degree of diligence required of banks is more than that of a good father of a family where the fiduciary nature of their relationship with their depositors is concerned.[17] Indeed, the banking

business is vested with the trust and confidence of the public; hence the appropriate standard of diligence must be very high, if not the highest, degree of diligence.[18] The standard applies, regardless of whether the account consists of only a few hundred pesos or of millions.[19]

The fiduciary nature of banking, previously imposed by case law,[20] is now enshrined in Republic Act No. 8791 or the General Banking Law of 2000. Section 2 of the law specifically says that the State recognizes the fiduciary nature of banking that requires high standards of integrity and performance.

Did petitioner treat respondents account with the highest degree of care? From all indications, it did not.

It is undisputed -- nay, even admitted -- that purportedly as an act of accommodation to a valued client, petitioner allowed the withdrawal of the face value of the deposited check prior to its clearing. That act certainly disregarded the clearance requirement of the banking system. Such a practice is unusual, because a check is not legal tender or money;[21] and its value can properly be transferred to a depositors account only after the check has been cleared by the drawee bank.[22]

Under ordinary banking practice, after receiving a check deposit, a bank *either* immediately credit the amount to a depositors account; *or* infuse value to that account only after the drawee bank shall have paid such amount.[23] Before the check shall have been cleared for deposit, the collecting bank can only assume at its own risk -- as herein petitioner did -- that the check would be cleared and paid out.

Reasonable business practice and prudence, moreover, dictated that petitioner should not have authorized the withdrawal by respondent of ₱240,000 on October 1, 1990, as this amount was over and above his outstanding cleared balance of ₱196,793.45.[24] Hence, the lower courts correctly appreciated the evidence in his favor.

Obligation as Collecting Agent

Indeed, the bank deposit slip expressed this reservation:

In receiving items on deposit, this Bank obligates itself only as the Depositors Collecting agent, assuming no responsibility beyond carefulness in selecting correspondents, and until such time as actual payments shall have come to its possession, this Bank reserves the right to charge back to the Depositors account any amounts previously credited whether or not the deposited item is returned. x x x."[25]

However, this reservation is not enough to insulate the bank from any liability. In the past, we have expressed doubt about the binding force of such conditions unilaterally imposed by a bank without the consent of the depositor.[26] It is indeed arguable that in signing the deposit slip, the depositor does so only to identify himself and not to agree to the conditions set forth at the back of the deposit slip.[27]

Further, by the express terms of the stipulation, petitioner took upon itself certain obligations as respondents agent, consonant with the well-settled rule that the relationship between the payee or holder of a commercial paper and the collecting bank is that of principal and agent.[28] Under Article 1909[29] of the Civil Code, such bank could be held liable not only for fraud, but also for negligence.

As a general rule, a bank is liable for the wrongful or tortuous acts and declarations of its officers or agents within the course and scope of their employment.[30] Due to the very nature of their business, banks are expected to exercise the highest degree of diligence in the selection and

supervision of their employees.[31] Jurisprudence has established that the lack of diligence of a servant is imputed to the negligence of the employer, when the negligent or wrongful act of the former proximately results in an injury to a third person;[32] in this case, the depositor.

The manager of the banks Cabanatuan branch, Consorcia Santiago, categorically admitted that she and the employees under her control had breached bank policies. They admittedly breached those policies when, without clearance from the drawee bank in Baguio, they allowed respondent to withdraw on October 1, 1990, the amount of the check deposited. Santiago testified that respondent was not officially informed about the debiting of the ₱101,000 from his existing balance of ₱170,000 on October 2, 1990 x x x.[33]

Being the branch manager, Santiago clearly acted within the scope of her authority in authorizing the withdrawal and the subsequent debiting without notice. Accordingly, what remains to be determined is whether her actions proximately caused respondents injury. Proximate cause is that which -- in a natural and continuous sequence, unbroken by any efficient intervening cause -- produces the injury, and without which the result would not have occurred.[34]

Let us go back to the facts as they unfolded. It is undeniable that the banks premature authorization of the withdrawal by respondent on October 1, 1990, triggered -- in rapid succession and in a natural sequence -- the debiting of his account, the fall of his account balance to insufficient levels, and the subsequent dishonor of his own checks for lack of funds. The CA correctly noted thus:

x x x [T]he depositor x x x withdrew his money upon the advice by [petitioner] that his money was already cleared. Without such advice, [respondent] would not have withdrawn the sum of ₱240,000.00. Therefore, it cannot be denied that it was [petitioners] fault which allowed [respondent] to withdraw a huge sum which he believed was already his.

To emphasize, it is beyond cavil that [respondent] had sufficient funds for the check. Had the ₱101,000.00 not [been] debited, the subject checks would not have been dishonored. Hence, we can say that [respondents] injury arose from the dishonor of his well-funded checks. x x x.[35]

Aggravating matters, petitioner failed to show that it had immediately and duly informed respondent of the debiting of his account. Nonetheless, it argues that the giving of notice was discernible from his act of depositing ₱50,000 on October 2, 1990, to augment his account and allow the debiting. This argument deserves short shrift.

First, notice was proper and ought to be expected. By the bank managers account, respondent was considered a valued client whose checks had always been sufficiently funded from 1987 to 1990,[36] until the October imbroglio. Thus, he deserved nothing less than an official notice of the precarious condition of his account.

Second, under the provisions of the Negotiable Instruments Law regarding the liability of a general indorser[37] and the procedure for a notice of dishonor,[38] it was incumbent on the bank to give proper notice to respondent. In *Gullas v. National Bank*,[39] the Court emphasized:

x x x [A] general indorser of a negotiable instrument engages that if the instrument the check in this case is dishonored and the necessary proceedings for its dishonor are duly taken, he will pay the amount thereof to the holder (Sec. 66) It has been held by a long line of authorities that notice of dishonor is necessary to charge an indorser and that the right of action against him does not accrue until the notice is given.

x x x. The fact we believe is undeniable that prior to the mailing of notice of dishonor, and without waiting for any action by Gullas, the bank made use of the money standing in his account to make good for the treasury warrant. *At this point recall that Gullas was merely an indorser and had issued checks in good faith. As to a depositor who has funds sufficient to meet payment of a check drawn by him in favor of a third party, it has been*

held that he has a right of action against the bank for its refusal to pay such a check in the absence of notice to him that the bank has applied the funds so deposited in extinguishment of past due claims held against him. (Callahan vs. Bank of Anderson [1904], 2 Ann. Cas., 203.) *However this may be, as to an indorser the situation is different, and notice should actually have been given him in order that he might protect his interests*.[40]

Third, regarding the deposit of ₱50,000 made by respondent on October 2, 1990, we fully subscribe to the CAs observations that it was not unusual for a well-reputed businessman like him, who ordinarily takes note of the amount of money he takes and releases, to immediately deposit money in his current account to answer for the postdated checks he had issued.[41]

Damages

Inasmuch as petitioner does not contest the basis for the award of damages and attorneys fees, we will no longer address these matters.

WHEREFORE, the Petition is *DENIED* and the assailed Decision *AFFIRMED*. Costs against petitioner.

SO ORDERED.

Sandoval-Gutierrez, Carpio-Morales, and *Garcia, JJ.,* concur.
Corona, J., on leave.

---

[1] *Rollo*, pp. 18-42.

[2] Penned by Justice Mercedes Gozo-Dadole and concurred in by Justices B. A. Adefuin de la Cruz (then Chairman, Ninth Division) and Mariano C. del Castillo.

[3] CA Decision, p. 9; *rollo*, p. 92.

[4] *Id.*, pp. 2-4 & 85-87. Citations omitted.

[5] The Petition was deemed submitted for decision on December 1, 2003, upon the courts receipt of respondents Memorandum signed by Atty. Cesar R. Villar. Petitioners Memorandum, signed by Atty. Edgardo G. Villarin, was received by the Court on November 5, 2003.

[6] Petitioners Memorandum, p. 8; *rollo*, p. 121.

[7] Aclon *v.* CA, 436 Phil. 219, 230, August 20, 2002; Reyes *v.* CA & Far East Bank and Trust Company, 415 Phil. 258, 267, August 15, 2001; W-Red Construction and Development Corporation *v.* CA, 392 Phil. 888, 894, August 17, 2000.

[8] Gullas *v.* National Bank, 62 Phil. 519, 521, November 13, 1935.

[9] Consolidated Bank & Trust Corporation *v.* CA, 410 SCRA 562, 574, September 11, 2003; Guingona Jr. *v.* City Fiscal of Manila, 128 SCRA 577, 584, April 4, 1984; Serrano *v.* Central Bank of the Phils., 96 SCRA 96, 102-103, February 14, 1980.

[10] Article 1278 provides:

Art. 1278. Compensation shall take place when two persons, in their own right, are creditors and debtors of each other. (See also Bank of the Philippine Islands *v.* CA, 325 Phil. 930, 938-939, March 29, 1996.)

[11] Article 1290 of the Civil Code.

[12] Article 1279 of the Civil Code.

[13] Gullas *v.* National Bank; *supra*, p. 522.

[14] GR No. 149454, May 28, 2004.

[15] *Id.*, per Panganiban, *J.*

[16] 336 Phil. 667, March 14, 1997 (cited in Reyes *v.* CA & Far East Bank and Trust Company; *supra*, p. 269.)

[17] *Id.*, p. 681, per Hermosisima Jr., *J.* See also Consolidated Bank & Trust Corporation *v.* CA; *supra*, pp. 574-575.

[18] Philippine Commercial International Bank *v.* CA, 350 SCRA 446, 472, January 29, 2001, per Quisumbing, J (citing Simex International (Manila), Inc. *v.* CA, 183 SCRA 360, 367, March 19, 1990).

[19] Prudential Bank *v.* CA, 384 Phil. 817, 825, March 16, 2000; Philippine National Bank *v.* CA, 373 Phil. 942, 948, September 28, 1999; Simex International *v.* CA, *supra*; BPI *v.* Intermediate Appellate Court, 206 SCRA 408, 412-413, February 21, 1992.

[20] Simex International *v.* CA, *supra*; BPI *v.* IAC, *supra*; Metropolitan Bank & Trust Co. *v.* CA, 237 SCRA 761, 767, October 26, 1994.

[21] Philippine Airlines, Inc. *v.* CA, 181 SCRA 557, 568, January 30, 1990.

[22] Roman Catholic Bishop of Malolos, Inc. *v.* IAC, 191 SCRA 411, 422, November 16, 1990 (cited in Bank of the Philippine Islands *v.* CA, 383 Phil. 538, 547, February 29, 2000).

[23] Bank of the Philippine Islands *v.* CA; *supra*, p. 554 (citing Banco Atlantico *v.* Auditor General, 81 SCRA 335, 340-341, January 31, 1978).

[24] This amount was computed based on the bank ledger which was submitted as Annex A of Respondents Complaint; *rollo*, p. 48.

[25] Petitioners (then Defendant-Appellants) Brief to the CA, pp. 5-6; *rollo*, pp. 62-63.

[26] Metropolitan Bank & Trust Company *v.* CA, 194 SCRA 169, 175, February 18, 1991.

[27] *Ibid.*

[28] Philippine Commercial International Bank *v.* CA; *supra*, p. 466.

[29] Art. 1909 of the Civil Code provides:

Art. 1909. The agent is responsible not only for fraud, but also for negligence, which shall be judged with more or less rigor by the courts, according to whether the agency was or was not for compensation.

[30] Philippine Commercial International Bank *v.* CA; *supra* at p. 470; Producers Bank of the Philippines (Now First International Bank) *v.* CA, 397 SCRA 651, 663, February 19, 2003. Article 2180 of the Civil Code, which embodies this principle, provides:

Art. 2180. The obligation imposed by Article 2176 is demandable not only for ones own acts or omissions, but also for those of persons for whom one is demandable.

x x x x x x x x x

Employers shall be liable for the damages caused by their employees and household helpers acting within the scope of their assigned tasks, even though the former are not engaged in any business or industry.

[31] Philippine Commercial International Bank *v.* CA; *supra*, p. 472.

[32] *Id.*, p. 464; BPI *v.* Casa Montessori Internationale; *supra*.

[33] RTC Decision, p. 4; *rollo*, p. 77.

[34] BPI *v.* Casa Montessori Internationale; *supra*, p. 26.

[35] CA Decision, pp. 7-8; *rollo*, pp. 90-91.

[36] RTC Decision, p. 3; *id.*, p. 76.

[37] 66 of the Negotiable Instruments Law provides:

Sec. 66. Liability of general indorser. Every indorser who indorses without qualification, warrants to all subsequent holders in due course:

x x x x x x x x x

And, in addition, he engages that, on due presentment, it shall be accepted or paid, or both, as the case may be, according to its tenor, and that if it be dishonored and the necessary proceedings on dishonor be duly taken, he will pay the amount thereof to the holder, or to any subsequent indorser who may be compelled to pay it.

[38] The procedure as to the manner and the time of giving notice is outlined under 89-118 of the said law. 89, in particular, provides as follows:

Sec. 89. To whom notice of dishonor must be given. Except as herein otherwise provided, when a negotiable instrument has been dishonored by non-acceptance or non-payment, notice of dishonor must be given to the drawer and to each indorser, and any drawer or indorser to whom such notice is not given is discharged.

[39] *Supra*.

[40] *Id.*, pp. 521-522, per Malcolm, *J*

[41] CA Decision, p. 7; *rollo*, p. 90.